

MERCER OLIVER WYMAN

Actuarial Consulting

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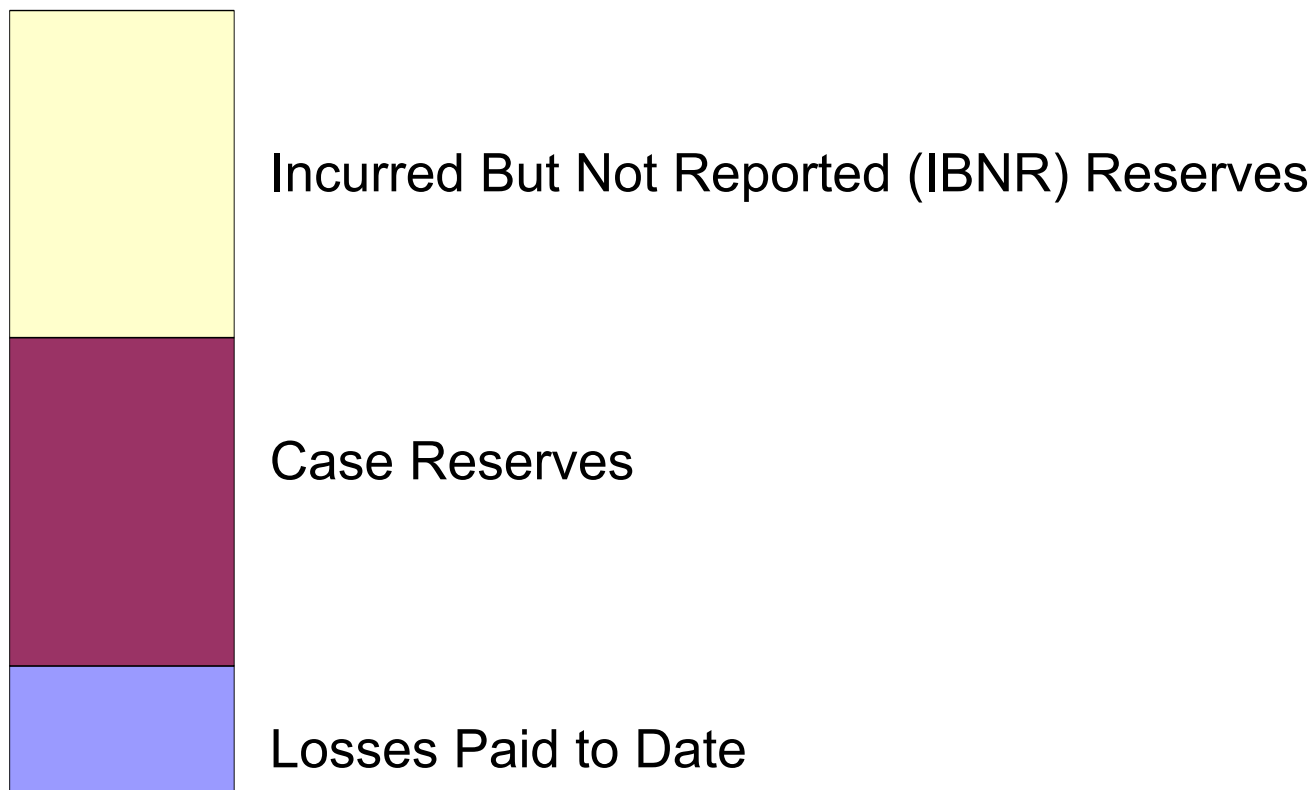
Medical Malpractice Insurance: The Importance of Loss Reserves

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Marsh & McLennan Companies

COMPONENTS OF TOTAL CLAIM COSTS



WHAT ARE LOSS RESERVES?

1) CASE RESERVES:

Estimates by claim professionals of future costs on reported claims based on known information.

2) INCURRED BUT NOT REPORTED RESERVES:

Actuarial forecasts of additional costs not included in case reserves.

HOW ARE CASE RESERVES ESTABLISHED?

A Case Reserve is an educated estimate of how much the future cost of a particular claim will be.

Based on:

- Experience of the claims professional;
- Information available at the time the reserve is established.

HOW ARE IBNR RESERVES ESTABLISHED?

Credentialed Actuaries rely on historical data to forecast future costs using established actuarial techniques and methodologies.

Forecasts must comply with:

- Casualty Actuarial Society
Statement of Principles Regarding Loss and Loss Adjustment Expense Reserves
- Casualty Actuarial Society
Code of Professional Conduct
- American Academy of Actuaries
Actuarial Standards of Practice

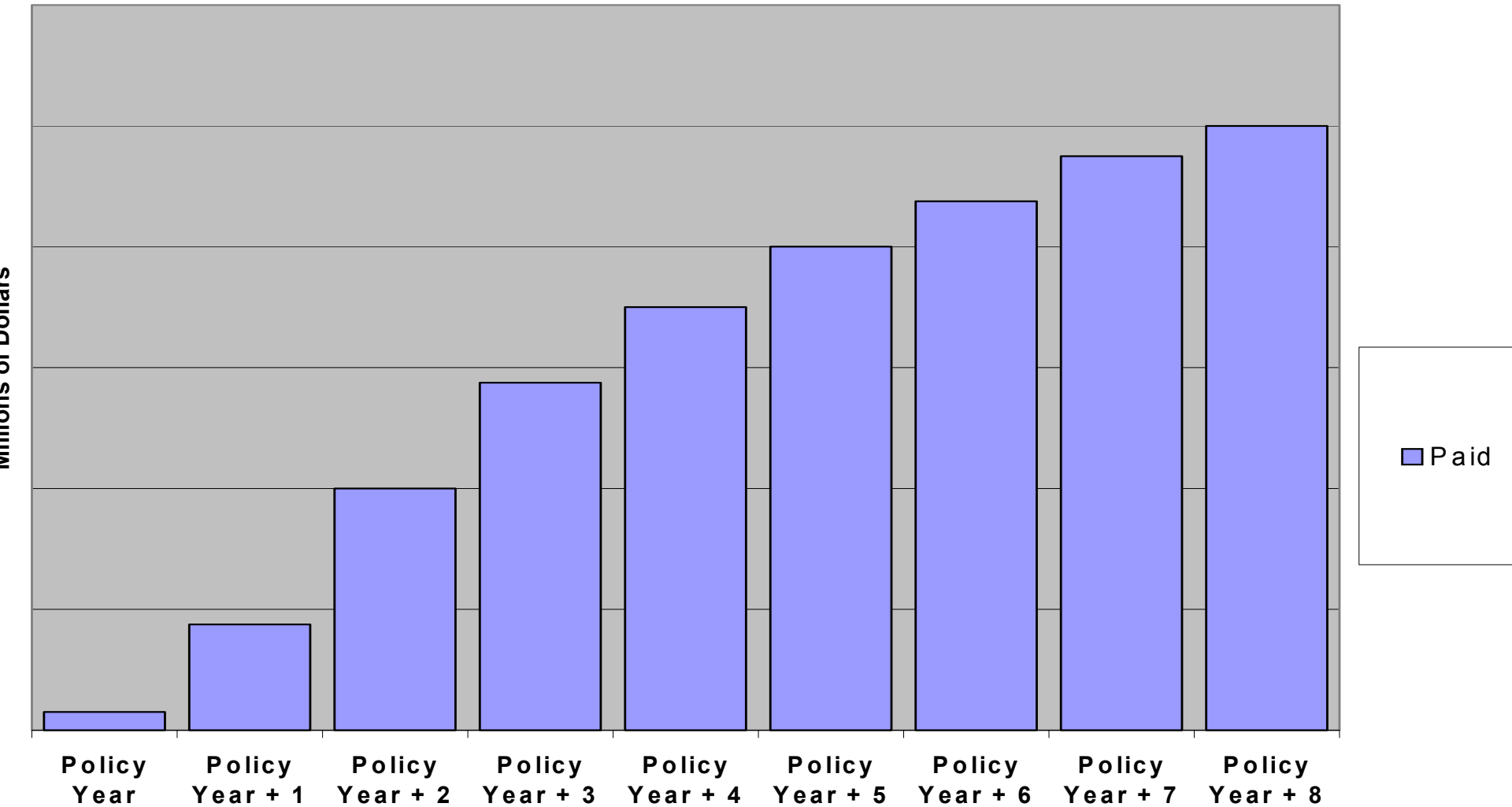
IMPORTANCE OF LOSS RESERVES

Medical Malpractice Insurance

- “Long-Tailed Line”.
- Claim payments made over many years.
- Approximately 3% of total costs are paid in year of coverage.
- Reserves are estimates of unpaid obligations.
- Adequate reserves ensure that funds are available to pay claims.
- Reserves cannot be dismissed as “speculative” or “discretionary”.

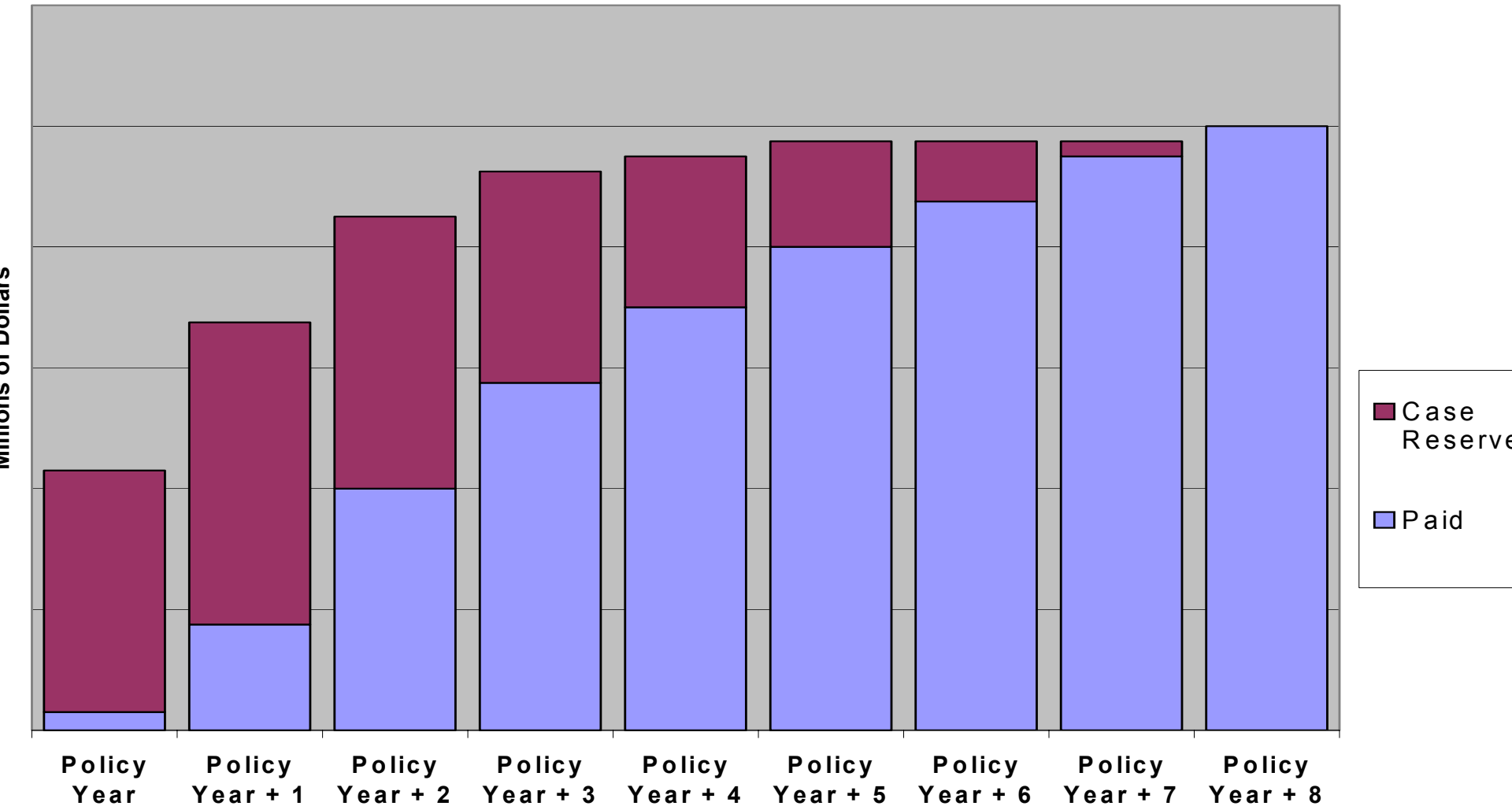
CHANGE IN CLAIM COSTS OVER TIME

The Theory



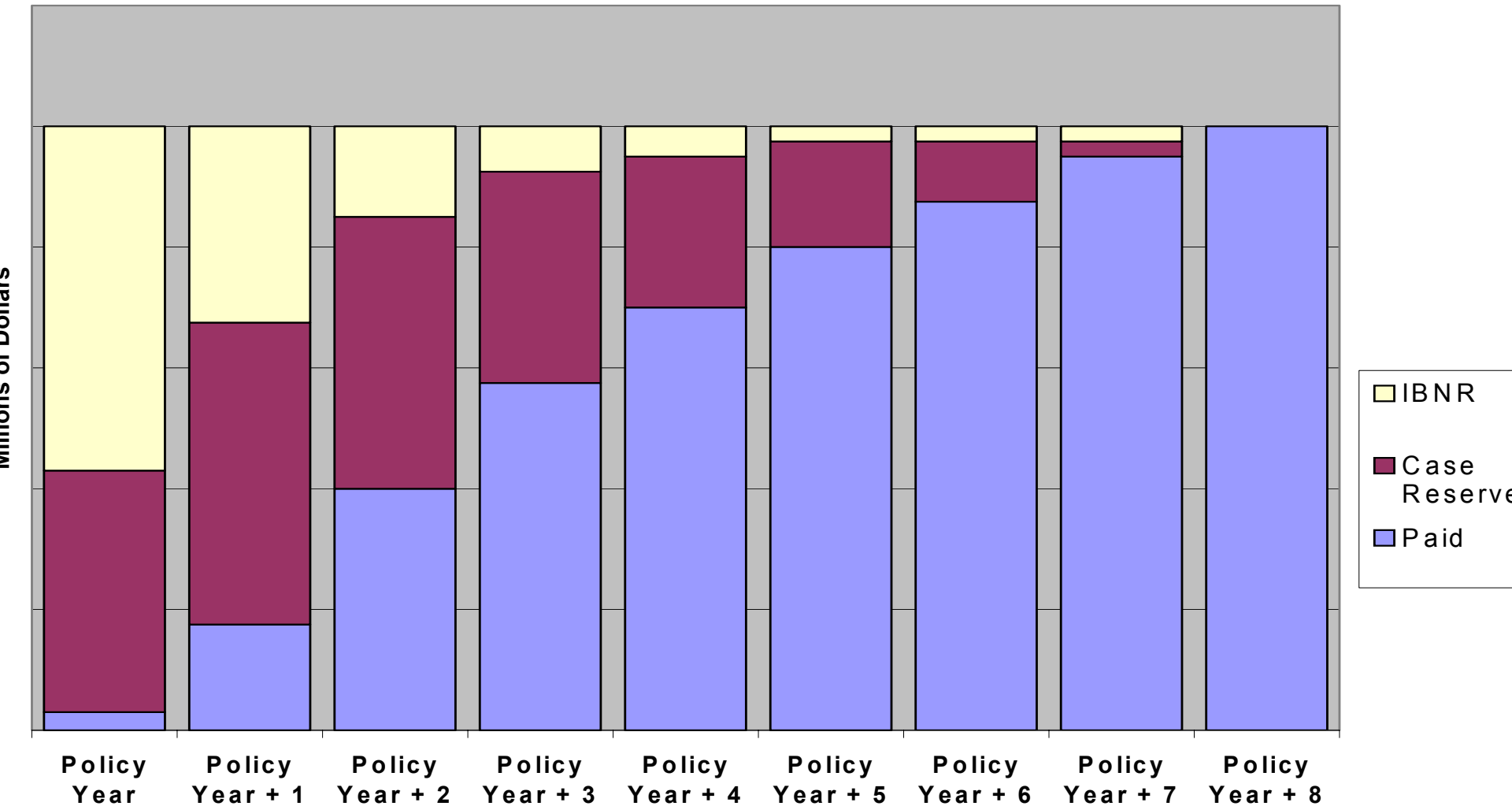
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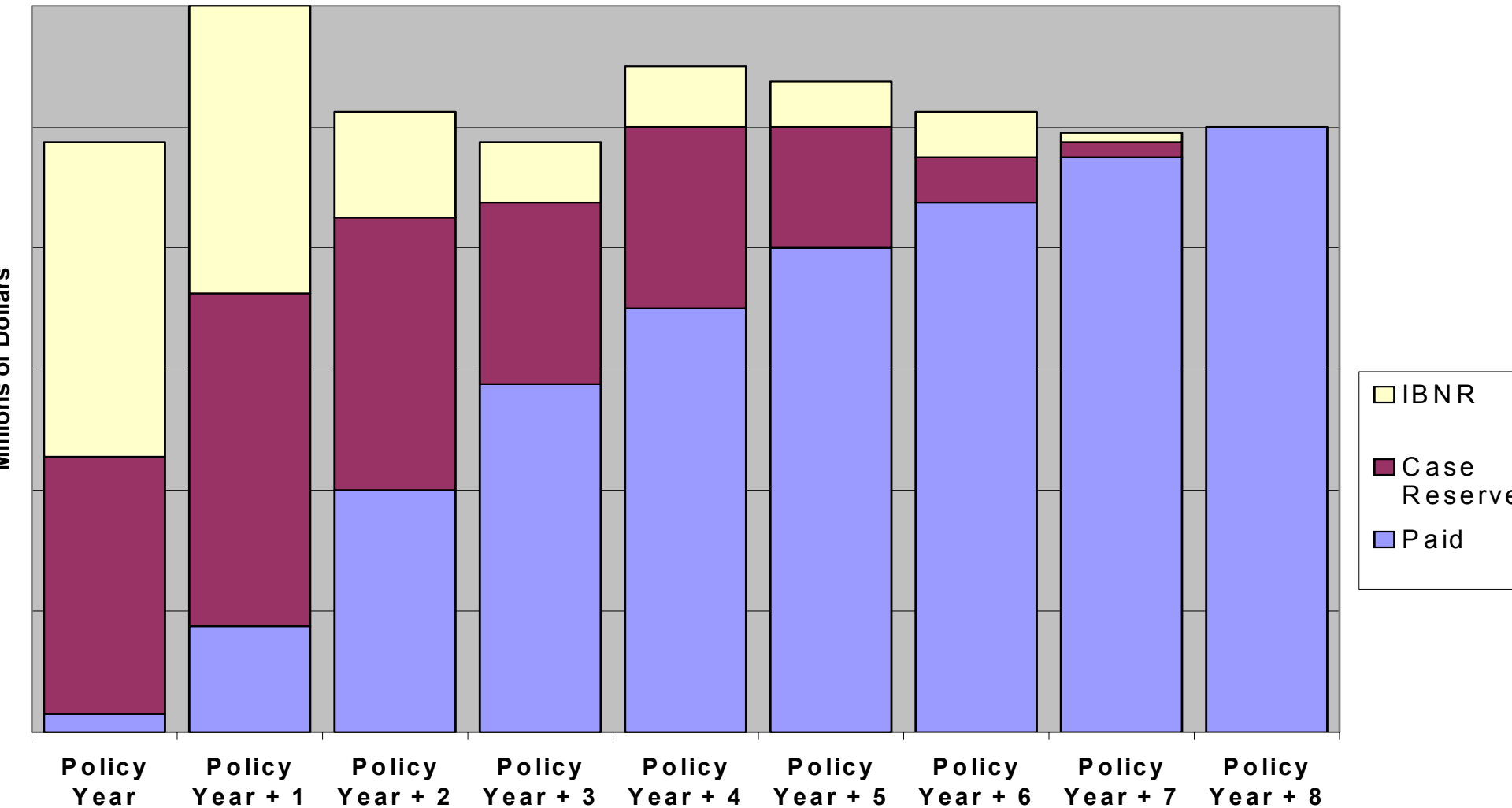
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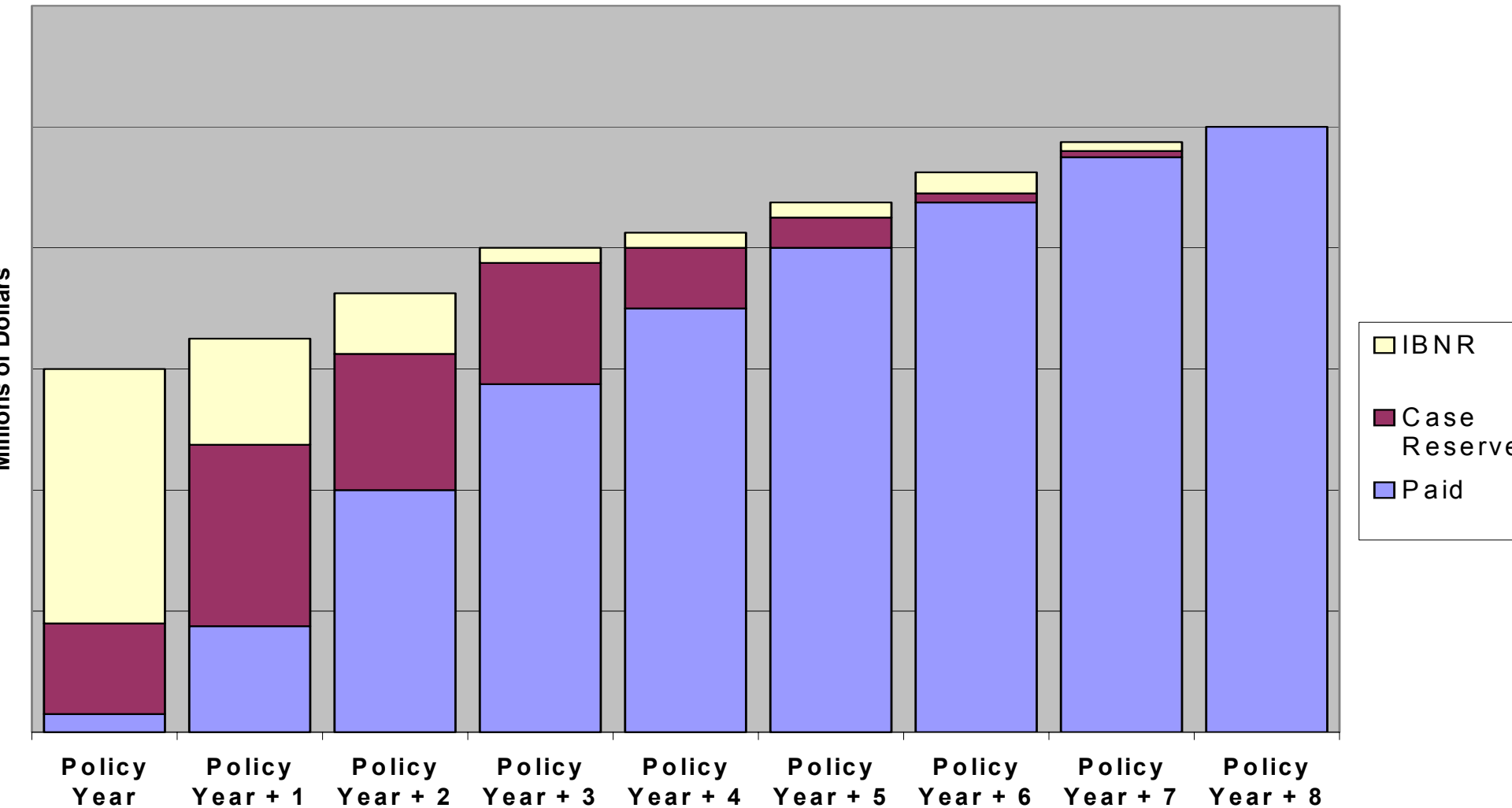
CHANGE IN CLAIM COSTS OVER TIME

What should happen



CHANGE IN CLAIM COSTS OVER TIME

What can happen



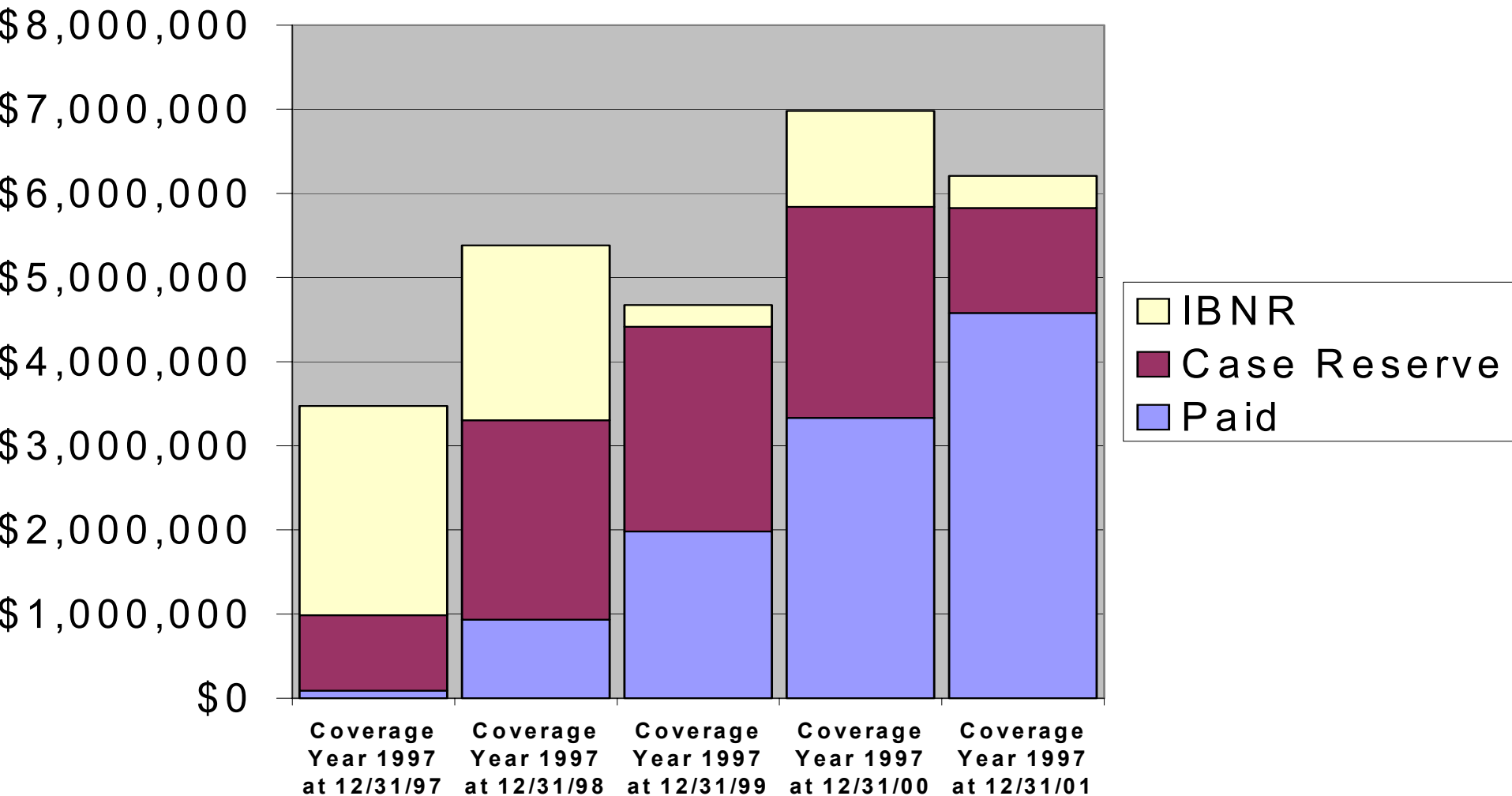
CASE STUDY:

Lawrenceville Property and Casualty Company

- Medical Malpractice Insurance Company domiciled in Virginia.
- Began writing medical malpractice policies in the end of 1996.
- Positive operating cash flow through 2001.
- Subsequently folded into parent company, MIIX Insurance Company (NJ), due to capital inadequacy and pressure from VA Insurance Regulators.
- MIIX has since stopped writing new business due to inadequate capital and pressure from NJ Insurance Regulators.
- Latest reserve estimates suggest that current assets and expected investment income will not be sufficient to fund MIIX's remaining policyholder obligations.

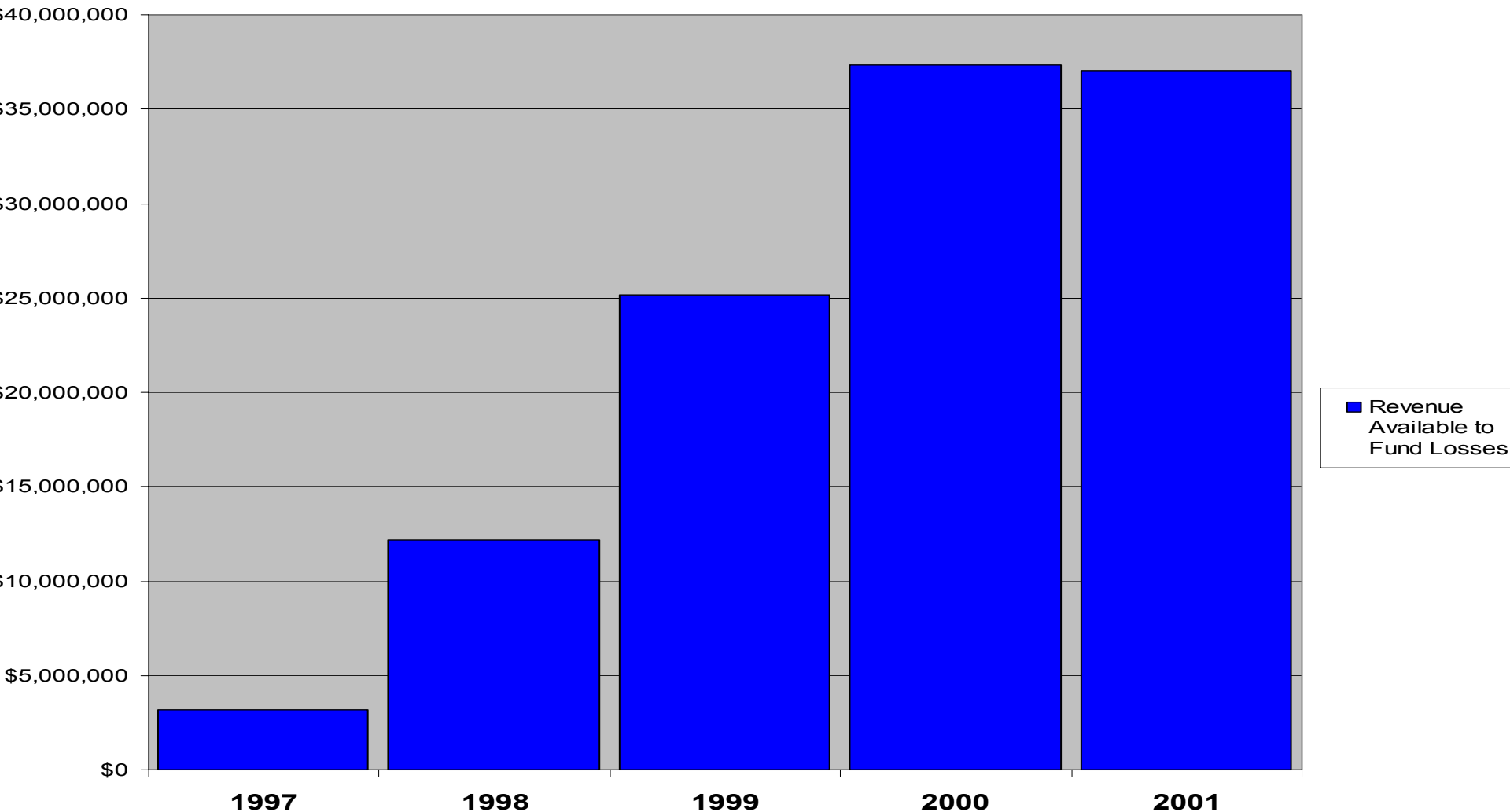
Lawrenceville Property and Casualty Company

Costs Due to 1997 Claims



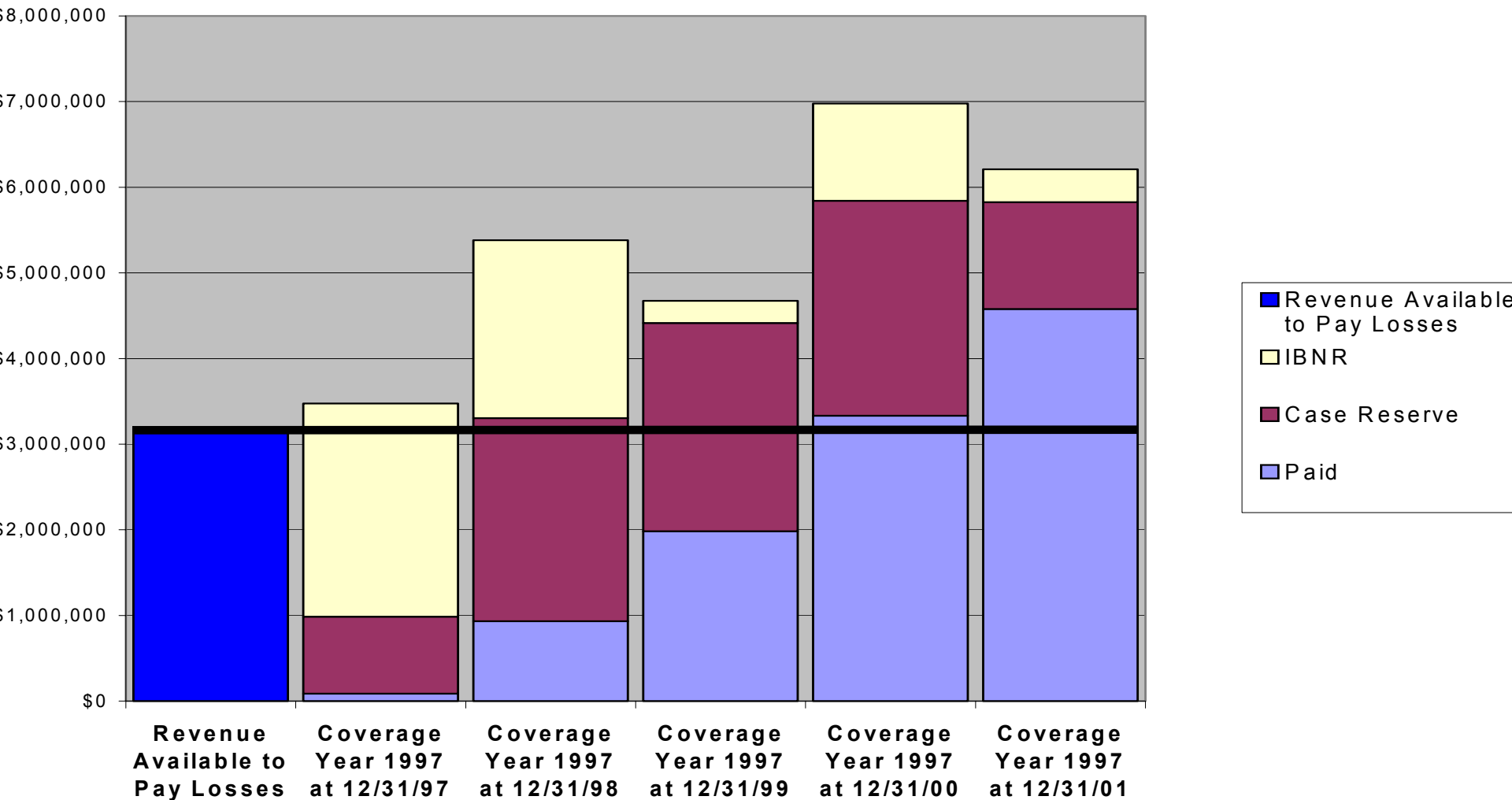
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Revenue Available to Fund Loss Payments



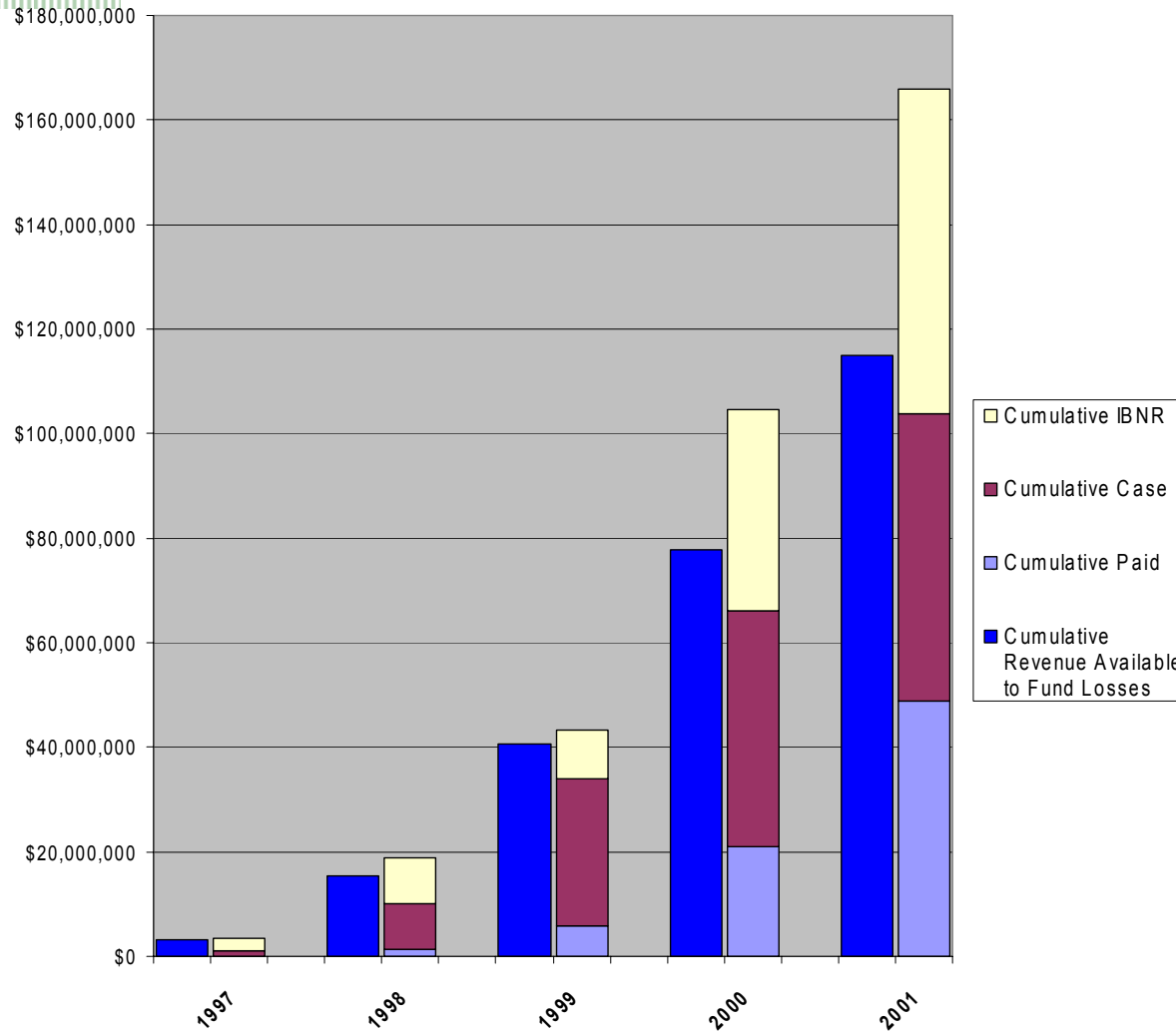
Lawrenceville Property and Casualty Company

Revenue Available to Fund Loss Payments displayed with Losses – 1997 claims



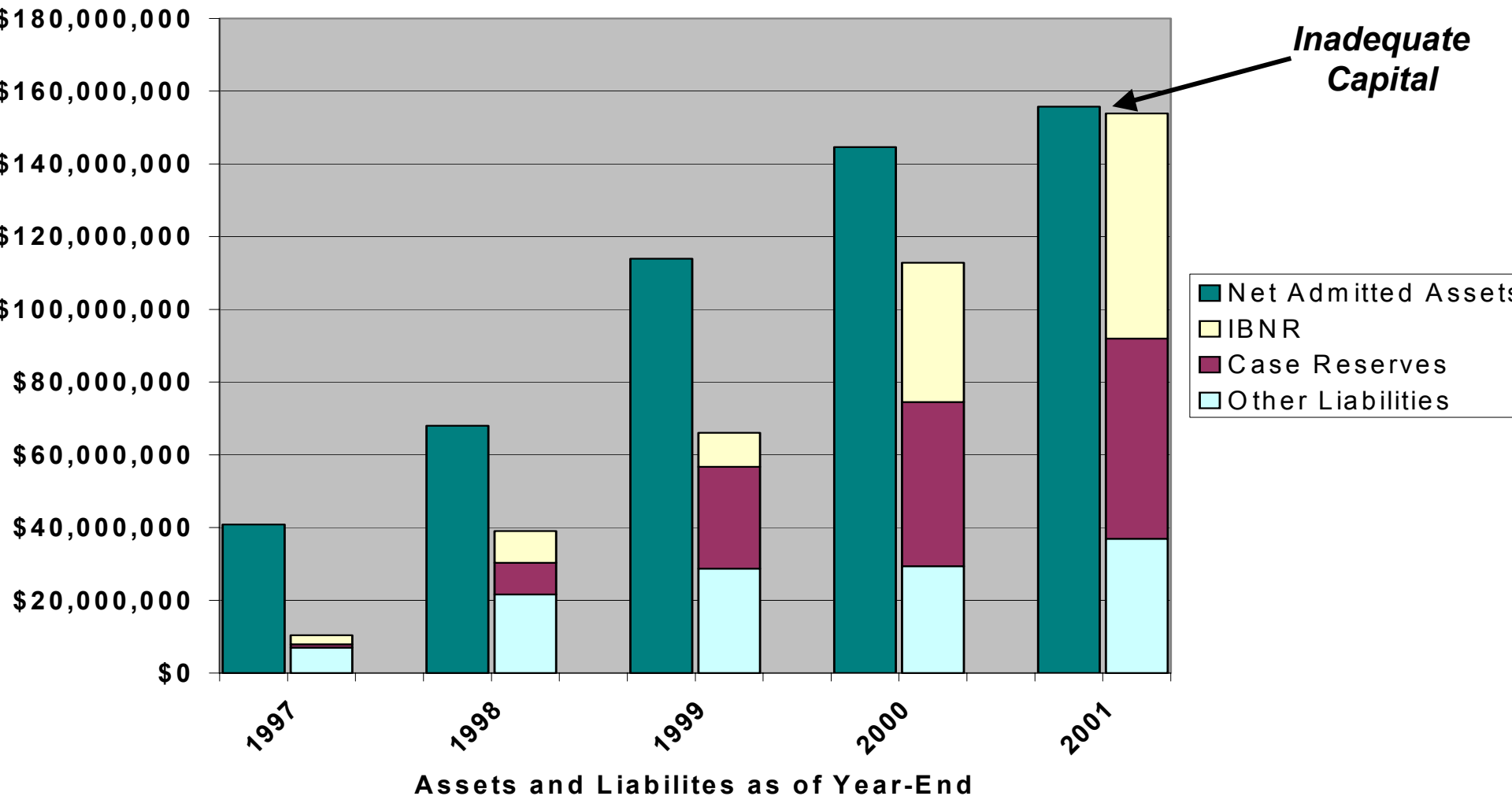
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Cumulative Revenue Available to Fund Loss Payments displayed with Cumulative Losses



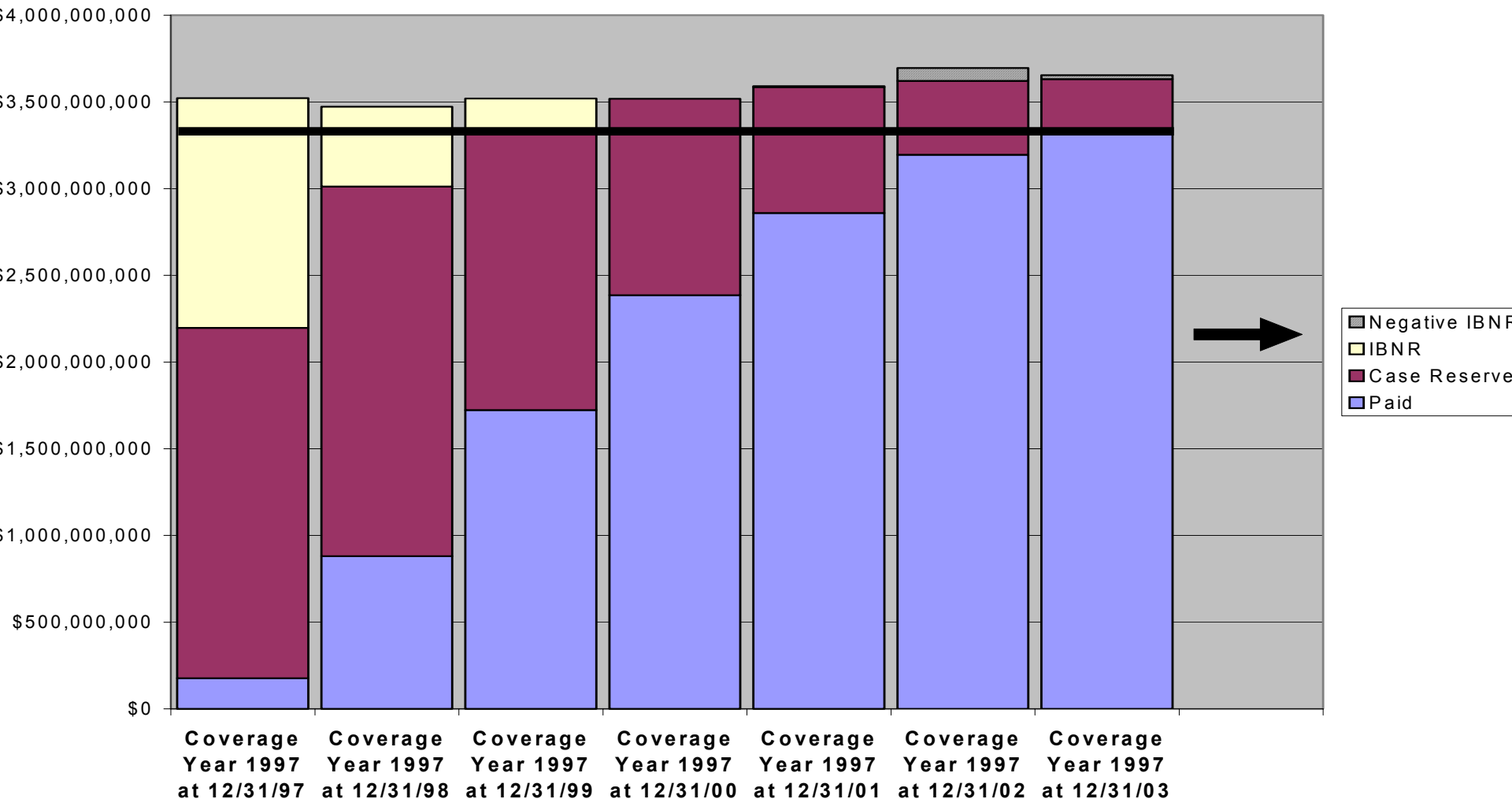
Lawrenceville Property and Casualty Company

Assets and Liabilities



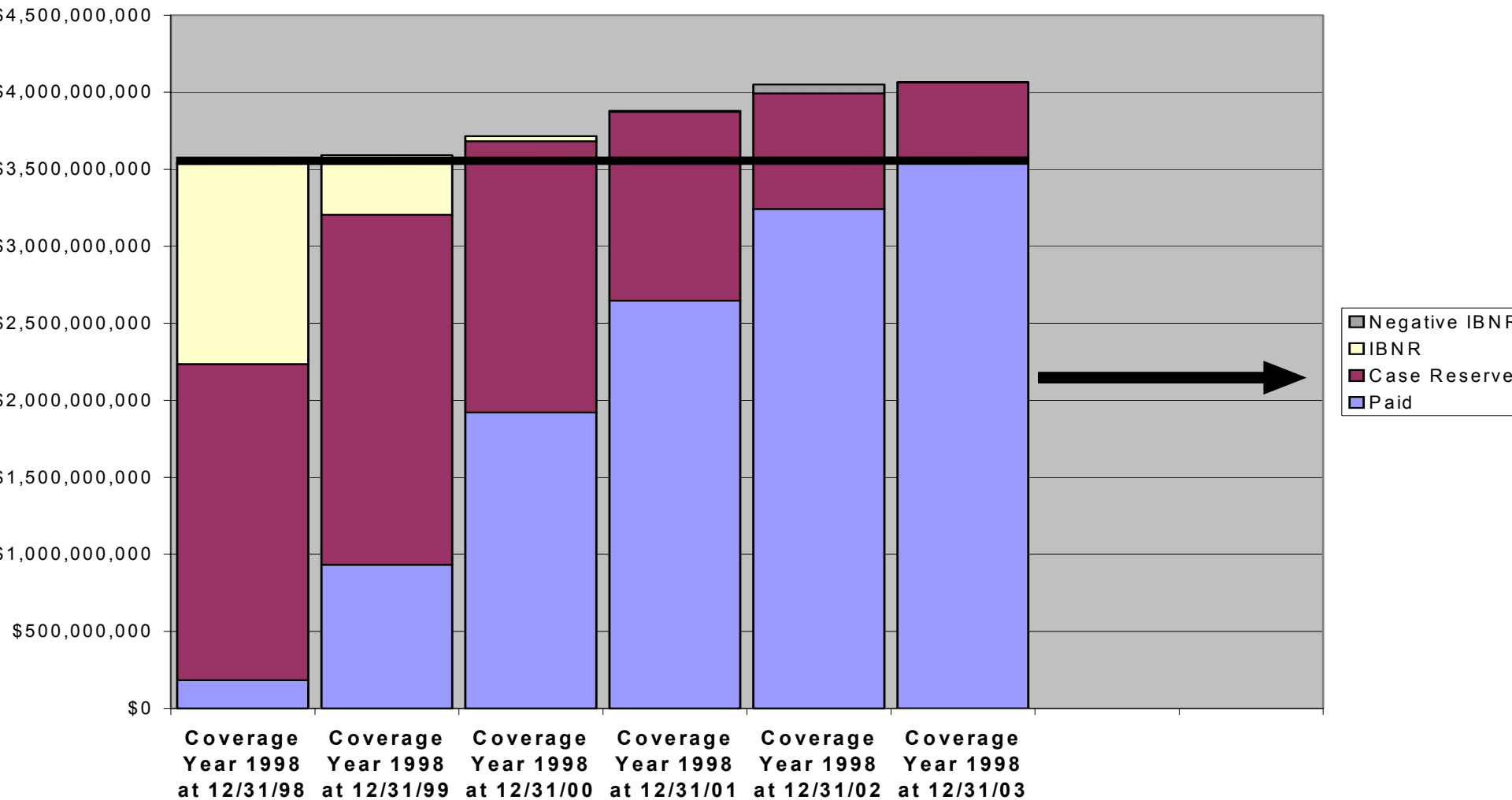
NOT LIMITED TO LAWRENCEVILLE AND MIIX

Industry-Wide Experience: 1997 Claims Made Med Mal



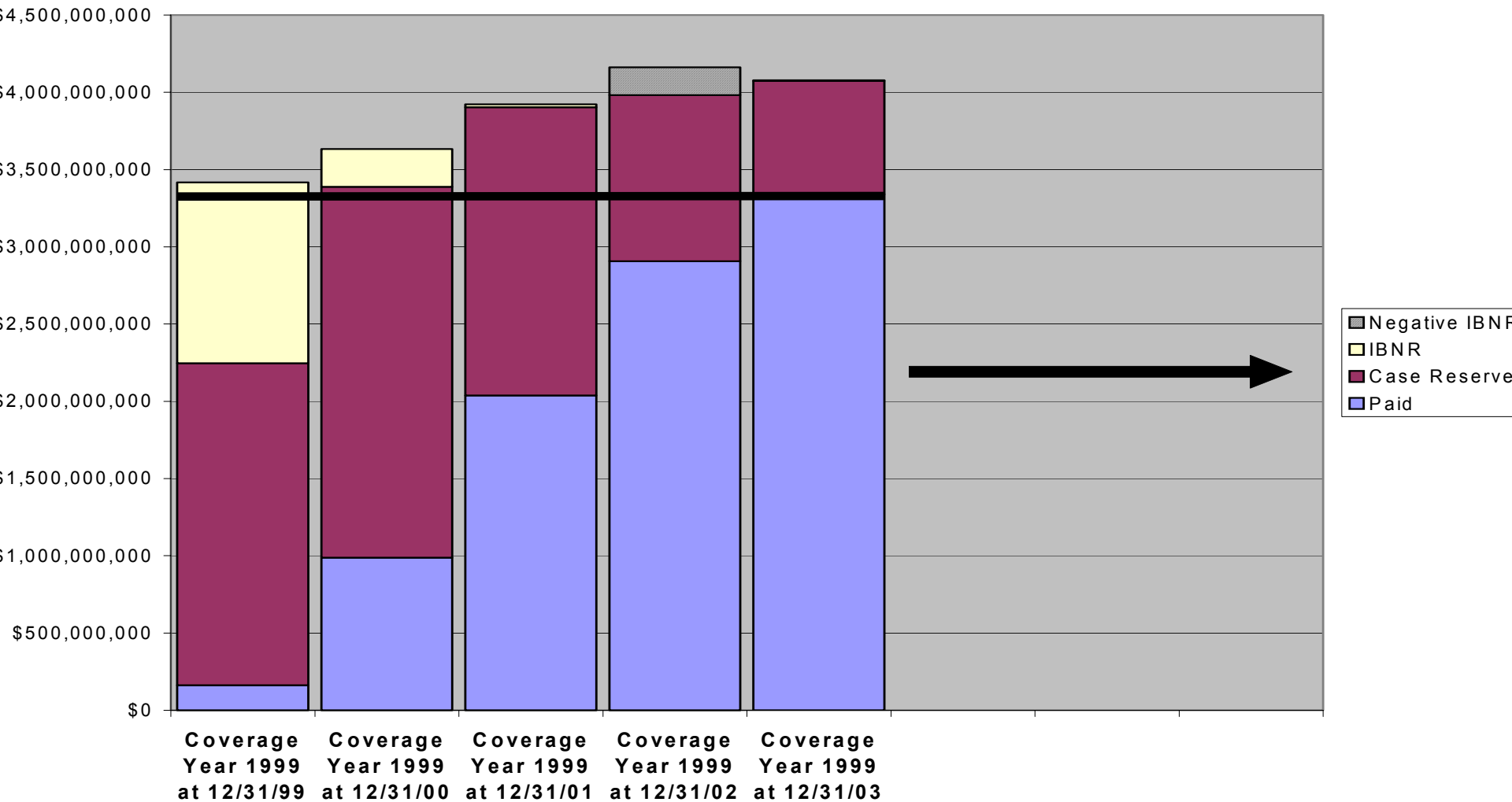
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Industry-Wide Experience: 1998 Claims Made Med Mal



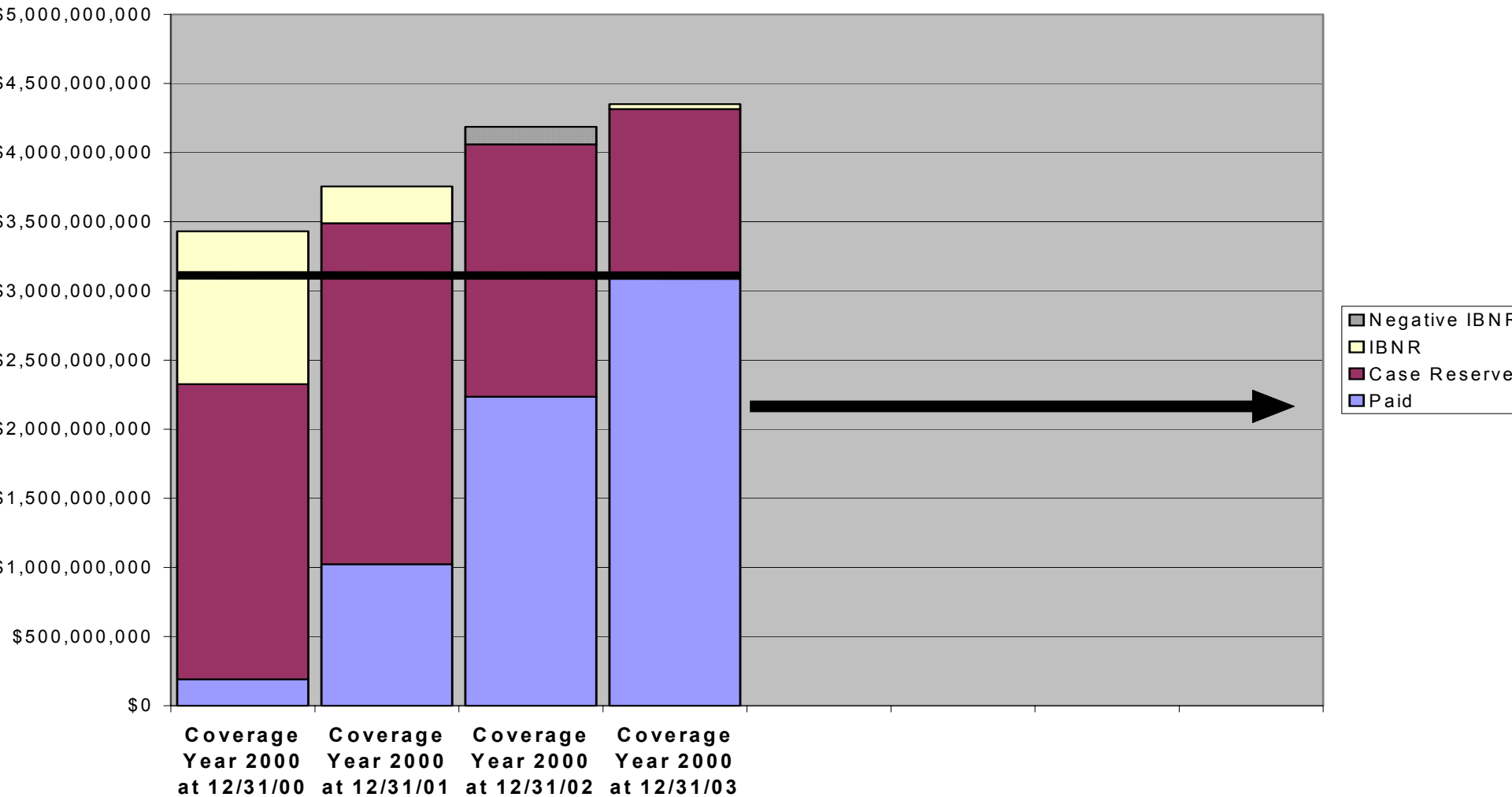
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Industry-Wide Experience: 1999 Claims Made Med Mal



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Industry-Wide Experience: 2000 Claims Made Med Mal



NOT LIMITED TO LAWRENCEVILLE AND MIIX

- In recent years, many companies have exited the medical malpractice market due to poor underwriting results.
- Some voluntary, some forced by regulatory action.
 - The Reciprocal Group
 - PHICO
 - Frontier
 - St. Paul